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IN THE
Supreme Court of the United States

OCTOBER TERM, 1982

HERBERT PATE and CAROLYN PATE,
Petitioners,

-vs.-

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERITORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Questions Presented for Review

1. Did the Second Circuit, in a criminal income tax evasion case, based upon the net worth or cash expenditures method of proof, violate this Court's holding in *Holland v. United States* which requires that, in such cases, the Government establish, with reasonable certainty, an opening net worth to serve as the starting point from which future increases in the taxpayer's assets are to be calculated?

2. Does the Second Circuit's holding that the Government is not obligated to negate all possible sources of nontaxable funds, in a criminal income tax evasion case based upon the net worth or cash expenditures method of proof where there is no proof of a likely source of income, directly conflict with its own prior decisions and decisions of this Court?

3. Did the trial Court, with respect to the conspiracy charge, commit reversible error in instructing the jury that it could determine whether the accused knowingly and wilfully entered into the alleged conspiracy from the acts and declarations of others?

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IN THE

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OCTOBER TERM, 1982

HERBERT PATE and CAROLYN PATE,
Petitioners,

-vs.-

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERITORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Herbert and Carolyn Pate, petitioners herein, pray that a writ of certiorari issue to review the judgment entered in this criminal case on July 20, 1982 by the United States Court of Appeals for the Second Circuit.

Opinions of the Courts Below

The opinion and judgment of the United States Court of Appeals for the Second Circuit sought to be reviewed is reproduced in Appendix A and is not yet officially reported.

Jurisdiction of the Supreme Court

The judgment of the United States Court of Appeals for the Second Circuit was entered on July 20, 1982. Title 28, United States Code, Section 1254(1) and Rule 22(2) of the United States Supreme Court Rules confer jurisdiction on this Court to review the judgment in question by a writ of certiorari.

Statutes Involved

Statutes:

Title 26, United States Code, §152(a) provides:

"(a) General definition. For purposes of this subtitle, the term 'dependent' means any of the following individuals over half of whose support, for the calendar year in which the taxable year of the taxpayer begins, was received from the taxpayer (or is received under subsection (c) or (e) as received from the taxpayer):

(1) A son or daughter of the taxpayer, or a descendant of either,

(2) A stepson or stepdaughter of the taxpayer,

(3) A brother, sister, stepbrother, or stepsister of the taxpayer,

(4) The father or mother of the taxpayer, or an ancestor of either,

(5) A stepfather or stepmother of the taxpayer,

(6) A son or daughter of a brother or sister of the taxpayer,

(7) A brother or sister of the father or mother of the taxpayer,

(8) A son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law of the taxpayer,

(9) An individual (other than an individual who at any time during the taxable year was the spouse, determined without regard to section 153, of the taxpayer) who, for the taxable year of the taxpayer, has as his principal place of abode the home of the taxpayer and is a member of the taxpayer's household, or,

. . . "

Rule 801(d)(2)(E), Federal Rules of Evidence, provides:

"(d) Statements which are not hearsay. A statement is not hearsay if —

(2) Admission by party-opponent. The statement is offered against a party and is . . . (E) a statement by a coconspirator of a party during the course and in furtherance of the conspiracy."

Statement of the Case

Introduction

The United States Court of Appeals for the Second Circuit, in the context of affirming petitioners' convictions, announced a new and drastically relaxed interpretation of the Government's burden of proof in a criminal tax case based upon the net worth or cash expenditures method of proof. Departing from all prior law, including its own decisional law, the Second Circuit has effectively ruled that it really is not necessary after all for the Govern-

ment to establish with reasonable certainty an opening net worth to serve as the starting point from which future increases in the taxpayer's assets are to be calculated.

The Second Circuit, contrary to previous holdings of this Court, has additionally ruled that in such a case the Government is not, in the absence of proof of a likely source of income, required to negate all possible nontaxable sources of income.

We submit that the Second Circuit's unwarranted relaxation of previously firmly established standards of proof is erroneous as it directly conflicts with all prior judicial constructions of the net worth or cash expenditures methods of proof as well as this Court's oft repeated caveat that courts closely scrutinize the Government's use of these circumstantial methods of proof as the basis for criminal tax prosecutions.

Also, in affirming petitioners' convictions, the Second Circuit has incredibly given its approval to jury instructions which, contrary to all prior decisional law, permitted the Government to prove the existence of the conspiratorial relationship between a declarant and the accused solely on the basis of the declarant's own bootstrap assertions.

Statement of Essential Facts

On April 13, 1978 Herbert and Carolyn Pate, the petitioners herein, were indicted and charged with wilfully and knowingly attempting to defraud the United States by filing an income tax return which substantially understated their income for 1971. Thereafter, on April 13, 1979, a second indictment was filed charging the Pates with wilfully and knowingly attempting to evade income taxes by failing

to file a tax return for 1972. A third indictment, filed on April 16, 1980, began with a count charging petitioners Herbert and Carolyn Pate, and Mr. Pate's attorney, Eugene Mastropieri, with conspiring with each other and with one Fiore Acovino to defraud the United States by obstructing the lawful income tax assessment and collection functions of the Internal Revenue Service (IRS). The third indictment also, to the extent relevant to this petition, charged the Pates with tax evasion by filing income tax returns which substantially understated their income for 1973, 1974 and 1975. Mr. Mastropieri was additionally charged with aiding and abetting these attempted evasions.

Following trial in the United States District Court for the Eastern District of New York before the Honorable Jacob Mishler and a jury, petitioners and co-defendant Mastropieri were convicted on all counts in which they were named except that Mr. Pate was acquitted of one count of the latter indictment, which is not relevant to this petition, and Mrs. Pate was acquitted of income tax evasion for 1972.

Mr. Pate has been sentenced to a total term of imprisonment of ten years. On the last of the three indictments he received concurrent terms of imprisonment of five years on Counts One, Five, Seven and Ten and three years on Counts Six and Eight. On the first two indictments Mr. Pate was sentenced to terms of imprisonment of five years to run concurrently with each other and with those in the third indictment. Finally, on Counts Two and Four, of the latter indictment, Mr. Pate was sentenced to prison terms of five years each, which sentences, while concurrent to each other, are consecutive to the other five year sentences imposed. Mrs. Pate was sentenced to a term of probation of two years.

On appeal to the United States Court of Appeals for the Second Circuit, Petitioners claimed that reversal of their convictions was mandated because of (i) the Government's failure to establish as to each of them the requisite starting point, (ii) the Government's failure to establish a likely source of income or negate any possible non-taxable funds, and because (iii) the District Court's jury instructions, concerning the law governing the conspiracy charge, constituted reversible error. On July 20, 1982 the Second Circuit, in a thirty-eight page opinion, affirmed petitioners convictions (Appendix A).

Reasons for Granting the Petition

POINT I

THE SECOND CIRCUIT'S ERRONEOUS RESOLUTION OF THE STARTING POINT ISSUE IS IN DIRECT CONFLICT WITH ITS OWN PRIOR DECISIONS, THIS COURT'S DECISIONS, AND THE RULINGS OF OTHER FEDERAL COURTS AND GIVEN THE INHERENT UNCERTAINTY OF PROOF IN SUCH CASES ESTABLISHES A DANGEROUS PRECEDENT

The Government's income tax prosecution of petitioners was based upon the net worth or cash expenditures method of proof. Consequently, the Government was obliged to establish with reasonable certainty, " . . . an opening net worth, to serve as a starting point from which to calculate future increases in the taxpayer's assets." *Holland v. United States*, 348 U.S. 121, 132 (1954); *United States v. Grasso*, 629 F.2d 805, 807 (2d Cir. 1980); *United States v. Costanzo*, 581 F.2d 29, 30 (2d Cir. 1978); *United States v. Penosi*, 452 F.2d 217 (5th Cir. 1971), *cert.*

denied, 405 U.S. 1065 (1972); *United States v. Balistrieri*, 403 F.2d 472, 479 (7th Cir. 1968).

Thus, the Government's proof must affirmatively show those assets on hand at the "starting point" and where its evidence fails to reasonably preclude the existence of other beginning point assets, an essential ingredient of a prima facie case is lacking. *United States v. Schipani*, 362 F.2d 825 (2d Cir.), *vacated per curiam on other grounds and reversed*, 385 U.S. 372 (1966); *Dupree v. United States*, 218 F.2d 781 (5th Cir. 1955), *reh. denied*, 220 F.2d 748 (1955); *United States v. Fenwick*, 177 F.2d 488 (7th Cir. 1949); *Bryan v. United States*, 173 F.2d 223 (5th Cir. 1949), *aff'd on other grounds*, 338 U.S. 552 (1950).

So firmly entrenched is this requirement that the Government establish with reasonable certainty an opening net worth that in 1954 this Court held:

> "Without proof that assets on hand at the beginning of the prosecution period did not account for the alleged net worth increases, the Government could not succeed." *Smith v. United States*, 348 U.S. 147, 155 (1954):

In the instant case, the Government arbitrarily selected January 1, 1971 as its starting point. It sought to supply the proof essential thereto by relying almost exclusively on a statement made by Herbert Pate, in July 1970, to one Sanford Eisler. According to Eisler's testimony, Mr. Pate stated in July, 1970, that he had no financial assets; that he had used up his funds for legal fees; and, that he had only a small sum in his checking account. There were no questions by Eisler regarding Mr. Pate's knowledge or understanding of Mrs. Pate's finan-

cial resources. In fact, there was virtually no reference to Mrs. Pate at all during their discussion. At Eisler's request, however, Mr. Pate filled out a written questionnaire in which he stated that since 1968 he and Mrs. Pate had owned a $10,000 life insurance policy. Mr. Eisler's trial testimony is fully set forth in Appendix B.

Thus, while statements by Mr. Pate concerning his wife's financial assets or resources would obviously not be binding upon her in any event, especially since the Eisler interview occurred prior to the operative dates of the alleged conspiracy, his only reference to her related to their joint ownership since 1968 of the $10,000 life insurance policy.[1]

The Government also relied on the underlying investigation, as conducted by the IRS agents, to determine and prove the Pates' assets on hand as of the January 1, 1971 starting point. However, there was no evidence that these investigative steps were undertaken for any year other than 1971 with the exception of the examination of local property records for "the years during the investigation", e.g. 1971-1975, "and prior to 1967."[2]

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1. Significantly, while Mr. Eisler, with respect to this written questionnaire, sought information regarding Mr. Pate's dependents, a spouse is not a "dependent" for income tax purposes. Title 26, United States Code, Section 152.

2. Oddly and without justification, the Second Circuit rejected petitioners' argument that "prior to 1967" literally means prior to 1967. Instead, the Court accepted the Government's claim that the words "prior to 1967" means from 1971 backwards to 1967. (Appendix A, p. 6a, fn. 4).

Since Mr. Pate's statement was limited to his own financial resources as of July, 1970 and since the IRS agents' investigation was itself limited almost exclusively to the year 1971, there was a critical and fatal gap in the Government's evidence regarding the January 1, 1971 starting point. There was no evidence that any investigation had been conducted for the period July, 1970 through December 31, 1970, to determine whether Mr. Pate's financial condition had changed during this time frame.[3]

Moreover, while it is undisputed that the Government knew that the Pates were separated during part of 1971, no effort was made to determine whether, or for how long, they had been separated prior to 1971. Nor was any evidence presented by the Government that an investigation had been conducted to determine the extent to which Mrs. Pate had income of her own from employment, or even alimony, prior to January 1, 1971.

Consequently, given the Government's complete failure of proof with respect to (i) the financial resources of Carolyn Pate prior to January 1, 1971 and (ii) the financial resources of Herbert Pate during the July, 1970 to December 31, 1970 time period, the Government's claim that the Pates *jointly* had no cash on hand as of the January 1, 1971 starting point is fatally and irrevocably flawed.

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3. Relevant portions of IRS Special Agent Patrick O. Conlisk's trial testimony concerning the scope of his investigation are set forth in Appendix C.

The Fifth Circuit, in reversing the net worth method conviction of a husband taxpayer, where joint tax returns had been filed, wrote:

> "Under its 'net worth' theory, however, the Government failed to establish with reasonable certainty a definite opening net worth of the joint income of Meriweather and his wife. Indeed, it came near ignoring Mrs. Meriweather." *United States v. Meriweather*, 440 F.2d 753, 755 (5th Cir. 1971).

The Second Circuit has confused the Government's obligation to establish, with reasonable certainty, the taxpayer's cash on hand position as of the starting point with the additional, but separate requirement that, the Government for the year in question, either establish a likely source of the allegedly unreported income or negate all possible non-taxable sources of funds. Since the Government selected January 1, 1971 as the starting point, common sense required that the focus of its investigation relative thereto be directed at the *pre* January 1, 1971 period. Here the Government chose simply to rely on Mr. Pate's July, 1970 statement to Mr. Eisler and there was no evidence that the IRS agents conducted any substantive investigation for the period prior to January 1, 1971. To the contrary, Agent Conlisk's trial testimony establishes that the Government's investigation, as it related to the Pates, was with two slight exceptions, limited to the year 1971.[4]

The Second Circuit, by affirming petitioners' convictions, has ignored the import of the Government's failure to negate the possibilities that (i) Mrs. Pate had pre-

4. The Second Circuit credited the Government with having checked local property records for the years 1967 through 1975 and the records of the Savings Bond division of the United States Treasury Department for the period "1947 or 1952" through 1975. (Appendix A, pp. 5a-6a).

January 1, 1971 assets, and (ii) that Mr. Pate's financial condition had, from non-taxable sources, changed during the period July, 1970 to December 31, 1970. In doing so, the Court has established a dangerous precedent regarding net worth or expenditures cases such as these, especially in light of this Court's admonition that:

> " . . . , careful study indicates that it is so fraught with danger for the innocent that the courts must closely scrutinize its use." *Holland v. United States, supra.* at 125.

Certiorari should be granted to review the Second Circuit's unwarranted departure from prior law and its undue relaxation of previously established standards governing elements to be proven in net worth or expenditures method income tax prosecutions.

POINT II

THE SECOND CIRCUIT'S DETERMINATION THAT THE GOVERNMENT IS NOT REQUIRED TO NEGATE ALL POSSIBLE NON-TAXABLE SOURCES OF FUNDS WHERE THERE IS NO EVIDENCE OF A LIKELY SOURCE OF INCOME IS IN DIRECT CONFLICT WITH ITS OWN PRIOR DECISIONS, THIS COURT'S DECISIONS AND THE RULINGS OF OTHER FEDERAL COURTS

At trial the Government conceded the absence of evidence regarding a likely source of the allegedly unreported income. Thus, as the Second Circuit had earlier written:

> "Either a 'likely source' of the illegally unreported income represented by the calculated increase in net worth plus non-deductible expenditures in the year in question

must be shown *or all possible sources of non-taxable income must be negated."* (emphasis supplied) *United States v. Grasso,* 629 F.2d 805, 807 (2d Cir. 1980).

In doing so the Second Circuit was simply relying on this Court's earlier pronouncement in *United States v. Masasei,* 355 U.S. 595 (1958):

> "In *Holland* we held that proof of a likely source was 'sufficient' to convict in a net worth case where the Government did not negative all the possible non-taxable sources of the alleged net worth increase. This was not intended to imply that proof of a likely source was necessary in every case. On the contrary, should *all possible* sources of non-taxable income be negatived, there would be no necessity of proof of a likely source."

The Second Circuit rejected the argument that the Government was required, absent proof of a likely source of income, to negate all possible nontaxable sources of income. It held that the Government was simply required to investigate "reasonably possible" sources of non-taxable income (Appendix A, p. 20a). Thus, the Second Circuit has not only ignored its own holdings in *Grasso, supra,* but also this Court's decisions in *Holland* and *Massei, supra.* Additionally, it has flatly disregarded similar holdings by other federal Courts having occasion to pass upon this issue. *United States v. Dworkin,* 644 F.2d 418, 422 (5th Cir. 1981); *United States v. Holovachka,* 314 F.2d 345, 357 (7th Cir. 1963); *United States v. Potts,* 321 F.Supp. 717 (E.D. Wisc. 1971).

The Second Circuit's reliance on *United States v. Bianco,* 534 F.2d 501, 506 (2d Cir. 1976) and *United States v. Schipani, supra.* at 830, for the proposition that the Government need only investigate "reasonably possible sources" of non-taxable funds is misplaced. In both of

those cases there was direct evidence of likely sources of unreported income. Yet, in this case, there was no such evidence. Thus, in *Bianco* and *Schipani* the Government went beyond what was required and conducted extensive investigations to rule out the possibility that the defendants had also received non-taxable funds, during the years in question. In this case, however, the Government's investigation was so totally lacking in thoroughness as to have drawn the Second Circuit's criticism. (Appendix A, p. 5a, fn. 3). See, *Lenski v. United States,* 383 F.2d 20, 23 (9th Cir. 1967).

Certiorari should be granted to correct the serious deviation from the uniform standards previously required by this Court governing net worth or expenditures method income tax prosecutions.

POINT III

THE DISTRICT COURT'S INSTRUCTIONS WHICH PERMITTED THE JURY TO DETERMINE PETITIONERS' MEMBERSHIP AND PARTICIPATION IN THE ALLEGED CONSPIRACY SOLELY ON THE BASIS OF ACTS AND STATEMENTS OF OTHERS CONSTITUTED REVERSIBLE ERROR

During petitioners' trial, the District Court, consistent with controlling precedent, made the threshhold determination that acts and declarations of alleged conspirators would be admitted against the others. *United States v. Geaney,* 417 F.2d 1116, 1119-1120 (2d Cir. 1969), *cert. denied sub nom. Lynch v. United States,* 397 U.S. 1028 (1970); Rule 104(a) and (b), Federal Rules of Evidence. Thereafter, however, over strenuous defense objection, the Court instructed the jury:

"If the Government proved the conspiracy charged in the indictment beyond a reasonable doubt, then you may use as evidence any act or declaration made by any individual who you find to be a member of the conspiracy against the accused in order to determine whether that accused knowingly and willfully entered into the conspiracy." (Appendix A, p. 12a).

This instruction is a patent misstatement of the law. *United States v. Ziegler*, 583 F.2d 77, 80 (2d Cir. 1978); *United States v. Geaney, supra.* Given this erroneous instruction, the jury, if it first found either Mr. Mastropieri or the unindicted Mr. Acovino to be a member of the conspiracy, was permitted to determine Mr. or Mrs. Pate's own membership in the conspiracy solely from Mastropieri or Acovino's own acts and declarations.

In 1978, the Second Circuit held:

> "The existence of a conspiratorial relationship between the declarant and the defendant must be established *aliunde* by independent evidence before the declarant's statements are admissible against the defendant. This rule rests on principles of the law of agency, where the *existence of the agency relationship cannot be proved by the alleged agent's own bootstrap assertion.*" (emphasis added)*United States v. Ziegler, supra.* at 79.

See also, *United States v. Gresko*, 632 F.2d 1128, 1131 (5th Cir. 1980); *United States v. Lutz*, 621 F.2d 940, 946-947 (9th Cir. 1980); *United States v. Petrozziello*, 548 F.2d 20, 22 (1st Cir. 1977); *Manual on Jury Instruction, Committee on Jury Instruction, Judicial Conference, 7th Cir.*, 36 F.R.D. 457, 502-504 (1962).

Not surprisingly, in affirming petitioners' convictions, the Second Circuit agreed that these instructions were clearly erroneous. Having done so, however, the

Court incorrectly observed that the only error with these instructions was the trial Court's omission of "the essential element" that declarations of a party to a conspiracy are admissible against another only if made in the course of and in furtherance of the conspiracy. (Appendix A, pp. 12a-13a).

Thus, the Second Circuit totally ignored the impact of the trial court's having incorrectly permitted the jury to determine Herbert or Carolyn Pate's membership in the charged conspiracy solely on the basis of acts or declarations of either Mr. Mastropieri or Mr. Acovino.

The Second Circuit correctly noted that since the trial Court had made the aforesaid independent threshhold determination of admissibility, no additional, or "second bite" instruction was required or necessary. (Appendix A, pp. 19a-20a). However, because of its failure to recognize the real vice and the implication of the trial Court's "clearly . . . erroneous" instruction; i.e., that the jury was permitted to determine both Mr. and Mrs. Pate's membership in the conspiracy solely on the basis of other alleged conspirators' acts and statements, the Second Circuit erroneously concluded that such error was harmless and, therefore, to be disregarded.

Indeed, its reliance on *United States v. Nickerson*, 606 F.2d 156, 158 (6th Cir.), *cert. denied*, 444 U.S. 994 (1979) for the proposition that such "second bite" instructions are universally favorable to the accused and, thus, constitute windfalls is misplaced. Simply stated, in *Nickerson* the jury was not, as it was in this case, permitted to

determine a defendant's membership in the conspiracy from statements of others.[5]

Since the trial Court's instruction in this case permitted the jury to consider the hearsay statements of co-conspirators without correctly outlining the legal requirements, the instruction constituted reversible error.

Certiorari should be granted to correct this important error.

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5. In *Nickerson, supra* at 157, the trial Court charged the jury, in pertinent part, as follows:

> ". . . whenever it appears beyond a reasonable doubt from the evidence in the case that a conspiracy did exist and that a defendant, . . . was a member of that conspiracy, then the statements thereafter made or knowingly made or the acts thereafter knowingly done in the furtherance of the conspiracy by any person likewise found to be a member of the conspiracy may be considered by the jury as evidence in the case as to the defendant found to have been a member of that conspiracy, . . ."

Thus, it was expressly required that the existence of the conspiratorial relationship between defendant and declarant be established *aliunde* by independent evidence before the jury was permitted to consider the declarant's acts or statements as against the defendant.

CONCLUSION

For the reasons stated herein, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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